

AR43

FATHOM

OCEANOLOGY LIMITED

1973

ANNUAL REPORT

FOR THE YEAR ENDED MARCH 31, 1973

Directors

- *K. R. OLSEN, Hudson, Quebec.
President, Fathom Oceanology Limited,
Vice President, Atlas Construction Limited.
 - *R. L. I. FJARLIE, Maxville, Ontario.
Executive Vice President, Fathom Oceanology Limited.
 - *N. E. HALE, Mississauga, Ontario.
Vice President Engineering, Fathom Oceanology Limited.
 - *J. B. FOOTE, Markham, Ontario.
Vice President, Assman Dictating Systems of Canada Ltd.
 - R. H. BRADSHAW, Toronto, Ontario.
Advertising and Sales Promotion Manager, The T. Eaton Company.
 - W. A. DOW, West Vancouver, British Columbia.
President, Ritchie Services Limited.
- *Member of the Executive Committee

Officers

- K. R. OLSEN, President
- R. L. I. FJARLIE, Executive Vice President
- N. E. HALE, Vice President
- K. GARDNER, Vice President
- J. O. EMPEY, Vice President
- B. G. CRANE, Controller
- R. A. DONALDSON, Secretary

Head Office and Plant

863 Rangeview Road, Port Credit, Ontario.

Subsidiary Company

Hale and Associates Limited, Port Credit, Ontario.

Transfer Agent and Registrar

National Trust Company Limited, Toronto, Ontario and Calgary, Alberta.

Banker

Bank of Montreal, Toronto, Ontario.

Auditors

Clarkson, Gordon & Co., Toronto, Ontario.

Legal Counsel

Blake, Cassels & Graydon, Toronto, Ontario.

The annual meeting of the shareholders of Fathom Oceanology Limited will be held in the Algonquin Room of the Royal York Hotel, Toronto at 2:00 P.M. on the 27th day of August 1973.

AR43

FATHOM
OCEANOLOGY LIMITED



SEMI-ANNUAL REPORT
TO SHAREHOLDERS
(UNAUDITED)

FOR SIX MONTHS ENDED
SEPTEMBER 30, 1973

SMITH

TO THE SHAREHOLDERS

Earnings for the six month period ended September 30, 1973 were \$9,643 or 1 cent per share. This compared with a loss of \$32,758 or 3 cents a share for the corresponding period a year ago. Revenue rose to a record \$414,903. Orders received during the period amounted to \$366,102 and the value of work on hand at October 1, was \$393,101.

Work continues in our plant on the two major systems for the Government of Brazil, one of which is now close to the assembly stage. The complete towing system for Columbia Gas of Ohio Inc. ordered last June has been finished. This system was shipped from the plant in Port Credit last month and within seven days it was installed, put through its sea trials and accepted by the customer.

On October 11 the company signed a contract with the Government of Canada enabling it to proceed with the first phase of a \$2,000,000 program designed to provide a very deep towing system for the Republic of West Germany.

Haare Olsen

K. R. OLSEN, P. Eng.
President.

November 6, 1973.

FATHOM OCEANOLOGY LIMITED
(Incorporated under the laws of Canada)

Consolidated Statement of Operations

For the Six Months Ended September 30th, 1973

with comparative figures for the Six Months Ended September 30th, 1972

Revenue	414,903	325,478
Costs		
Manufacturing	345,554	280,140
Administrative	120,923	125,824
Less recovery of costs - D.I.P. program	466,477	405,964
Net cost	61,217	47,728
Earnings (loss)	405,260	358,236
Per share	9,643	(32,758)
	\$0.01	\$ (0.03)

Consolidated Statement of Changes in Financial Position

For the Six Months Ended September 30th, 1973

with comparative figures for the Six Months Ended September 30th, 1972

FUNDS WERE RECEIVED FROM	1973	1972*
Operations	\$	\$
Net earnings (loss) for the period	9,643	(32,758)
Add charges to operations not involving an outlay of working capital, Depreciation and amortization	22,800	28,450
Funds provided by operations	32,443	(4,308)
Proceeds from O.D.C. loan	32,443	100,000
Total funds received	32,443	95,692

FUNDS WERE APPLIED TO	1973	1972*
Reduction in long term debt	2,738	6,385
Purchase of fixed assets	40,625	3,737
Cost of patents	10,040	5,915
Total funds applied	53,403	16,037
DECREASE (INCREASE) IN WORKING CAPITAL	20,960	(79,655)
WORKING CAPITAL	95,750	37,978
Beginning of period	74,790	117,633
End of period		

*The 1972 figures have been restated to conform to the 1973 basis of presentation.

FATHOM OCEANOLOGY LIMITED

(Incorporated under the laws of Canada)

To the Shareholders of Fathom Oceanology Limited

Summary of Results

The operating results of the company continue to improve. Annual losses have steadily declined as progress has been made and a break even point was reached for the first time in late fiscal 1973 with a modest profit showing in the final months. Losses for the whole year amounted to \$29,250 or 2½ cents a share all of which occurred in the first nine months. This compares with \$95,000 or 9 cents a share last year and \$264,000 or 27 cents a share for the year before.

While operating revenue rose 4 percent to \$441,000 from \$425,000, administrative costs were reduced by 32 percent and manufacturing costs by 16 percent with a total cost reduction of \$167,905 or 19.4 percent from the last fiscal year.

Completed Contracts and Work in Progress

The company closed some 30 contracts during the year of which the most significant was the system for the Royal Swedish Navy. This project was completed in July 1972. Other contracts include a study for the U.S. Navy on towed submarine antenna systems and fairings for the Ministry of Transport for an experimental application of faired cables for moored buoys in tidal waters. We also received orders for spare parts for systems in service and for replacement fairings.

The most significant contract of those in progress is the one for the two towing systems for the Government of Brazil. The design work is complete, some of the components are in production and the first of the two systems will undergo shop tests in October 1973. One system will be delivered early in 1974 and the other in 1975.

The value of work on hand on April 1, 1973 was \$579,000. This compares with \$650,000 on the same date in 1972.

The Outlook

When Fathom began business four years ago its largest single problem was to convince customers and investors that it knew its business. Three years later it had partly achieved this objective by producing two commercial systems for a large customer in the oil industry.

While this achievement impressed some of its critics, it was still a considerable jump from producing a low speed commercial system to the building of a large high speed military towing system capable of withstanding the rigors of naval operations.

The opportunity to meet this challenge came from the Royal Swedish Navy in 1971 and last July the first Fathom military system was delivered. It is a matter of record that it was accepted without reservation and of interest to note that subsequent to its official tests it was also successfully subjected last November to a week of storm conditions in the Kattegat area off the west coast of Sweden.

This news travelled fast. Among the senior personnel of the world's navies there appears to be a relationship that permits the rapid exchange of information of this kind, for the success of the Fathom system quickly became known all over the world.

A film made by the customer during the Swedish trials was put at Fathom's disposal and this has already been seen by eager audiences of naval people from most of the major nations.

With all this achievement, what is our future? As this report goes to press we have bids outstanding worth some ten million dollars. Potential customers for complete systems have, for the most part, made up their minds about the Fathom part of their needed equipment but it must be noted that a complete facility also needs electronic counterparts that we do not make. There are several major international companies in this business and we work with them all. The electronic part of the system represents by far the

Fitting patented Fathom 'Flexnose' fairing to an experimental cable. The exclusive hydrodynamic design of the fairings permits higher towing speeds than can be obtained with any other known fairing.

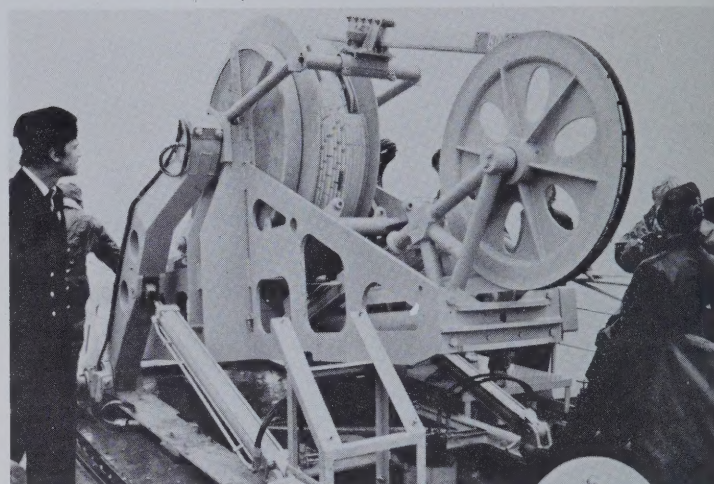


largest dollar part of the total contract and it is the electronic supplier who usually becomes our actual customer. When the end user buys, he buys from the electronic system supplier and he in turn places business with us. We have little choice but to wait for this to happen. We can now say without fear of contradiction that the Fathom system is unique and accepted.

Financial Position

While our financial position has improved, it cannot be considered as satisfactory. We have come a long way since our formation some four and a half years ago but it has been expensive. We believe that we are now close to a stable and profitable operation.

Our confidence in the future is shared by both the Federal Government and the Government of Ontario, both of whom have shown financial interest. This interest was not given without considerable investigation and it may be of some comfort to shareholders to know that we have survived such close scrutiny. Fathom is a high technology company with a unique product that is needed by what can only be described as blue chip international clients of the very highest quality.



Photograph taken during trials by the Royal Swedish Navy in the Baltic Sea.

Our day-to-day financial obligations are being met and expenses of all kinds come under the closest examination. Only modest compensation is being paid the most senior company officials and we have recently sublet an unused part of our plant in Port Credit to help defray costs there.

We have a very close association with our banker, The Bank of Montreal, and its help and sound advice is invaluable to us at this time.

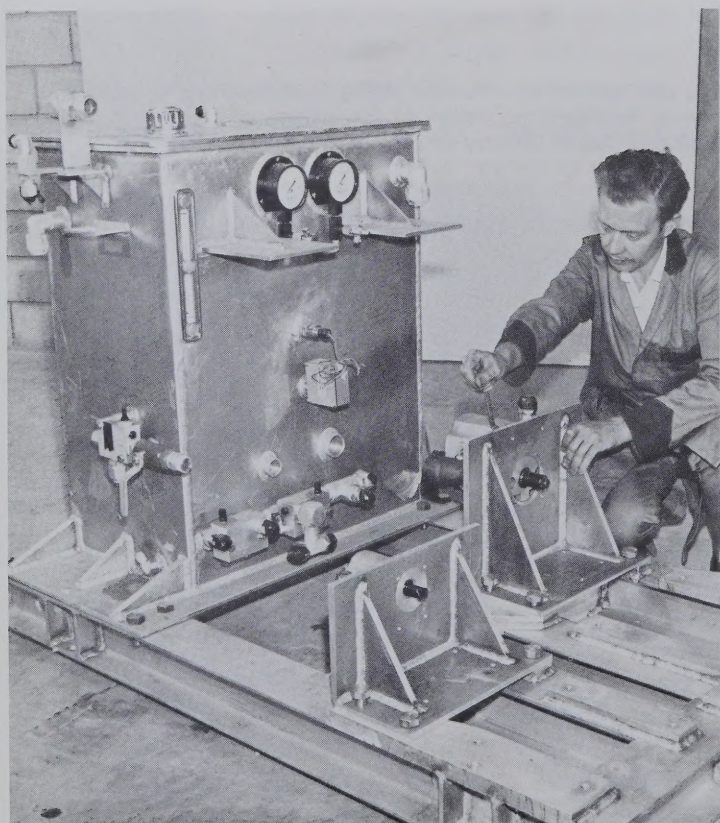
Staff

Total number of people on staff at the close of the financial year was twenty-two. They are all very capable people and have developed into a strong team with specific and well identified objectives. They are the company and the Directors must take this annual opportunity of publicly recognizing and thanking them for their loyal and enthusiastic service.

By Order of the Board of Directors,

K. R. Olsen

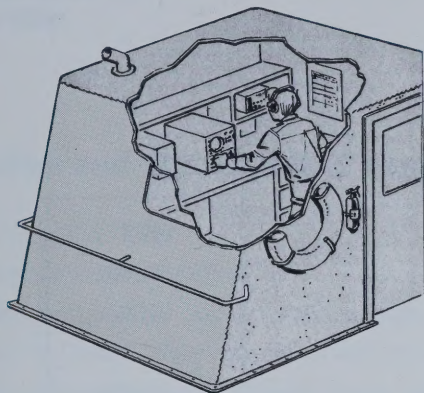
K. R. Olsen
President



One of the hydraulic power units for the Brazilian Navy contract photographed in the Fathom plant in Port Credit, Ontario.

The complete system . . .

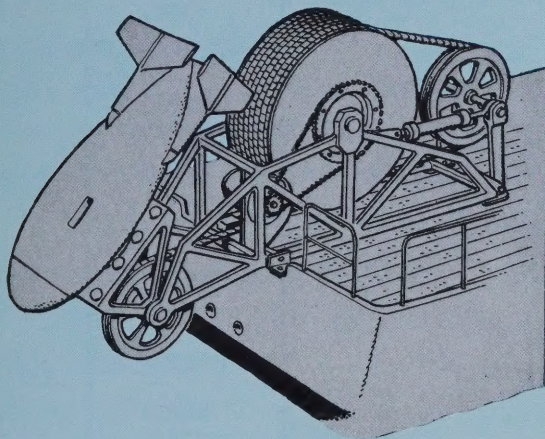
The part made by others



The data room on board ship

Several large international companies make and supply this equipment.

The part made by Fathom



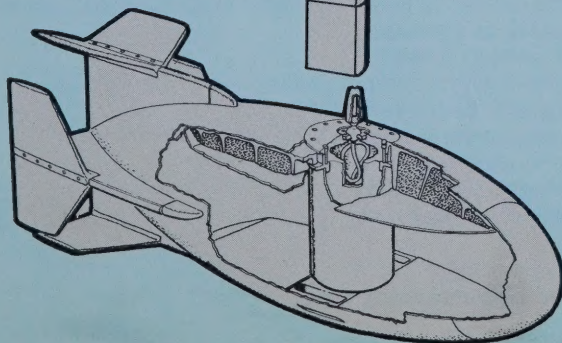
The launching, towing and recovery machinery on board ship

Only available from Fathom and used to control the towed fish.



Faired cable holding towed fish

Faired cable as such can come from a number of sources. Fathom has designed and holds patents on a fairing that has unique hydrodynamic qualities that permit cable to be acceptably controlled at much higher speeds than any other fairing manufacturer has been able to obtain.



The towed fish

Has hydrodynamic characteristics and is used to hold appropriate electronic equipment for sensing.

FATHOM OCEANOLOGY LIMITED

(Incorporated under the laws of Canada)

Consolidated Balance with comparative figures

Assets

CURRENT ASSETS:

	1973	1972
Short-term deposit (note 3)	\$150,000	—
Accounts receivable (notes 4 and 7(a))	12,682	\$142,024
Grants receivable from Government of Canada—		
D.I.P. (note 5)	35,979	62,565
I.R.D.I.A.	73,154	35,000
Costs and estimated earnings in excess of billings on uncompleted contracts (note 2)	34,686	94,450
Inventory, at lower of cost and net realizable value	43,910	15,241
Prepaid expenses and travel advances	9,922	7,837
Total current assets	<u>360,333</u>	<u>357,117</u>

FIXED ASSETS (note 6)

99,837 113,032

OTHER:

Patents and patents pending, at amortized cost (note 2)	84,417	74,245
Completed engineering designs, at nominal value	1	1
Rent deposits	<u>10,213</u>	<u>10,238</u>
Total other assets	<u>94,631</u>	<u>84,484</u>

Total assets \$554,801 \$554,633

On behalf of the Board:

K. R. OLSEN, Director

R. L. I. FJARLIE, Director

(See accompanying notes to Consolidated Financial Statements)

Liabilities and Shareholders' Equity

CURRENT LIABILITIES:

	1973	1972
Bank indebtedness (note 4)	\$ 56,168	\$129,198
Accounts payable and accrued charges	73,247	158,518
Due to Ontario Development Corporation—export support loan (note 7(a))	117,357	—
12% convertible notes payable (note 7(b))	6,000	25,000
Employee income and other taxes payable	4,733	6,423
Current portion of venture capital loan	7,078	—
Total current liabilities	<u>264,583</u>	<u>319,139</u>

NON-CURRENT LIABILITIES:

12% convertible notes payable (note 7)	184,050	175,350
Due to shareholders (note 7(b))	—	14,850
Due to Ontario Development Corporation—venture capital loan (note 7(a))	90,133	—
Total non-current liabilities	<u>274,183</u>	<u>190,200</u>

MINORITY INTEREST (note 9(b))	<u>12,480</u>	<u>12,480</u>
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SHAREHOLDERS' EQUITY

Share capital (note 8)		
Authorized:		
2,000,000 common shares without nominal or par value		
Issued:		
1,181,667 common shares	512,622	512,622
Deficit (statement 2)	<u>(509,067)</u>	<u>(479,808)</u>
Total shareholders' equity	<u>3,555</u>	<u>32,814</u>
Total liabilities and shareholders' equity	<u>\$554,801</u>	<u>\$554,633</u>

Auditors' Report

To the Shareholders of
 FATHOM OCEANOLOGY LIMITED

We have examined the consolidated balance sheet of Fathom Oceanology Limited and its subsidiary as at March 31, 1973, and the consolidated statements of operations and deficit and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position

of the companies as at March 31, 1973, the results of their operations and the changes in their financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
 June 19, 1973

CLARKSON, GORDON & CO.
 Chartered Accountants

Consolidated Statement of Operations and Deficit
for the year ended March 31, 1973
with comparative figures for the year ended March 31, 1972

(Statement 2)

	1973	1972*
REVENUE	✓ \$440,788	✓ \$424,850
COSTS:		
Manufacturing	446,786	532,086
Administrative	212,689	311,860
Interest—long-term	26,049	7,612
Interest—short-term	<u>12,255</u>	<u>14,126</u>
	697,779	865,684
LESS RECOVERY OF COSTS—		
Grants from Government of Canada:		
D.I.P. program (note 5)	(187,537)	(311,169)
I.R.D.I.A. program	<u>(40,195)</u>	<u>(35,000)</u>
Net costs	<u>470,047</u>	<u>519,515</u>
NET LOSS FOR THE YEAR	✓ 29,259	✓ 94,665
DEFICIT, BEGINNING OF YEAR	<u>479,808</u>	<u>385,143</u>
DEFICIT, END OF YEAR	<u>\$509,067</u>	<u>\$479,808</u>
NET LOSS PER SHARE	<u>\$.025</u>	<u>\$.09</u>

*The 1972 figures have been restated to conform to the 1973 basis of presentation.

FATHOM OCEANOLOGY LIMITED

(Incorporated under the laws of Canada)

Consolidated Statement of Changes in Financial Position

(Statement 3)

for the year ended March 31, 1973

with comparative figures for the year ended March 31, 1972

	1973	1972
FUNDS WERE RECEIVED FROM:		
Proceeds from D.I.P. grant for fixed assets (note 5)	\$ 12,297	\$ 30,279
Proceeds from Ontario Development Corporation venture capital loan (net less current portion of \$7,078)	90,133	—
Proceeds from issue of 12% convertible notes payable (note 7(b))	—	200,350
Transfer of shareholders' loans to non-current liabilities	—	14,850
Proceeds from disposal of fixed assets	1,413	3,755
Total funds received	<u>103,843</u>	<u>249,234</u>
FUNDS WERE APPLIED TO:		
Operations—		
Net loss for the year	29,259	94,665
Less charges to operations not involving an outlay of working capital:		
Depreciation and amortization of fixed assets	(33,059)	(37,181)
Amortization of patents and patents pending	(5,086)	(3,857)
Other	(58)	(1,785)
Funds (received from) applied to operations	(8,944)	51,842
Transfer of 12% note to current liabilities (note 7(b))	6,000	25,000
Purchase of fixed assets	33,607	113,456
Cost of patents and patents pending	15,258	2,287
Other	150	50
Total funds applied	<u>46,071</u>	<u>192,635</u>
INCREASE in working capital	57,772	56,599
WORKING CAPITAL (DEFICIT), beginning of year	37,978	(18,621)
WORKING CAPITAL, end of year	<u>\$ 95,750</u>	<u>\$ 37,978</u>
REPRESENTED BY:		
Current assets	\$360,333	\$357,117
Current liabilities	264,583	319,139
	<u>\$ 95,750</u>	<u>\$ 37,978</u>

(See accompanying notes to Consolidated Financial Statements)

FATHOM OCEANOLOGY LIMITED

(Incorporated under the laws of Canada)

Notes to Consolidated Financial Statements March 31, 1973

1. Principles of consolidation

The consolidated financial statements include the accounts of Fathom Oceanology Limited and its partially-owned subsidiary Hale & Associates Limited from the date of acquisition on May 1, 1969.

2. Accounting practice

The general practice followed by the company for contract work is to record profits on contracts in progress by the percentage of completion method, giving full recognition to losses when they become known. In the case of contracts extending over one or more years, revisions in cost and profit estimates, which can be significant, are reflected in the accounting period in which the relevant facts become known.

The accounting practice followed by the company for research and development costs, excluding costs of patents and patents pending, is to expense these items in the year. The company amortizes the cost of patents and patents pending in a systematic manner, the 1971 costs in proportion to projected sales over the period to March 31, 1978 and subsequent additions evenly over 10 years.

3. Short-term deposit

Under the terms of a contract in progress, the company is required to provide a letter of credit as a performance bond. The letter of credit is fully secured by a short-term bank deposit of \$150,000 at March 31, 1973. The bank deposit is only released as specified portions of the contract are completed up to January 1974.

4. Bank indebtedness

The bank loan is partially secured by a general assignment of those book debts not assigned to the Ontario Development Corporation. Reference is made to note 7(a).

5. Research and development

On February 24, 1972 the company contracted with the Government of Canada under the D.I.P. program to continue the design and development of its towing systems. The Department agreed to contribute 50% of defined expenditures by the company on this project before July 1974. Under the terms of the contract the amount contributed by the Government shall not exceed \$602,500, of which \$187,537 (in respect of operating costs) has been reflected in the statement of operations in 1973 (\$311,169 in 1972) and \$42,576 (in respect of fixed assets) has been reflected as a reduction in the cost of fixed assets on the balance sheet. While the Government is contributing these funds, in certain circumstances it can require partial or complete repayment of the grant. With Government approval, the company, rather than repaying the grants, can reinvest the funds in future development projects.

6. Fixed assets

	Original cost	Government grant (note 5)	Accumulated depreciation and amortization	Net book value	
				1973	1972
Equipment	\$ 47,123	—	\$21,492	\$25,631	\$ 27,834
Ship ocean simulator	60,850	\$30,279	11,004	19,567	24,168
Automobiles	—	—	—	—	118
Leasehold improvements	25,638	—	8,359	17,279	19,131
Patterns and tooling	101,397	12,297	51,740	37,360	41,781
	<u>\$235,008</u>	<u>\$42,576</u>	<u>\$92,595</u>		
Total fixed assets				<u>\$99,837</u>	<u>\$113,032</u>

7. Long-term debt

(a) Ontario Development Corporation—

During the year the company entered into an agreement with the Ontario Development Corporation (O.D.C.) under which O.D.C. agreed to advance an 8% venture capital loan of \$100,000 and a 6½% export support loan of \$150,000. The venture capital loan is being repaid over 10 years in blended monthly payments of principal and interest of \$1,206. The export support loan is to provide funds to finance export sales and is repayable on demand.

The loans are secured by:

- chattel mortgage on all equipment owned by the company,
- a floating charge on all other assets (except accounts receivable required to secure any bank loans),
- an assignment and postponement for ten years of 12% convertible notes outstanding at May 31, 1972 as described in note 7(b),

- an assignment of fire and export insurance policies,
- an assignment of specific accounts receivable related to sales financed under the export support loan program.

(b) 12% convertible notes—

Under the terms of an agreement signed by the noteholders in favour of the Ontario Development Corporation, the 12% convertible notes cannot be redeemed until all loans from the Ontario Development Corporation have been repaid, with the exception of two notes totalling \$6,000 which are repayable on December 1, 1973. Reference is made to note 7(a). The notes are convertible at a price of \$0.60 per share in whole or in part, at the option of the noteholder, into fully-paid and non-assessable shares of the company.

At a meeting of August 24, 1972, the directors authorized a change in the conversion rate on \$35,000 of the notes from \$0.90 per share to \$0.60 per share.

At a meeting on May 31, 1972, the directors approved the conversion of \$14,700 of the non-interest bearing loans due to shareholders into 12% convertible notes, which notes are convertible at \$0.60 per share.

8. Share capital

200,000 shares have been reserved under the terms of a stock option plan for senior officers (150,000 shares) and key employees (50,000 shares). At a meeting on April 6, 1972, the directors agreed to amend the option price of \$1.00 per share under the plan, to an amount equal to 90% of the market value of the shares on the date of granting the options. Accordingly, a 15,000 share option granted to a senior officer of the company was cancelled and replaced by an option of 15,000 shares at an option price of \$0.405 (90% of \$0.45) and a further option on 15,000 shares was granted to an officer at the same option price. On May 31, 1972 the company granted options on 50,000 shares to two officers of the company and 45,000 shares to key employees at an option price of \$0.405. All of the share options are exercisable in the following percentages commencing with the date the option is granted.

	Percentage of original option exercisable
During the 1st year of option	33 $\frac{1}{3}$ %
During the 2nd year of option	66 $\frac{2}{3}$ %
During the 3rd year of option	100 %
The company has reserved the following unissued common shares:	
For stock options	200,000 shares
For 12% convertible notes payable (note 7(b))	316,750 shares
For minority interest in subsidiary (note 9(b))	4,160 shares
	<u>520,910 shares</u>

9. Commitments

At March 31, 1973 the company:

- (a) had a commitment under a premises lease to pay rent at an annual rate of approximately \$30,000 up to November 30, 1979; and
- (b) had an agreement with certain shareholders to purchase the balance of the shares of the partially-owned subsidiary for \$12,480, when and if these shareholders are able to acquire the shares. The agreement provides that the purchase price of \$12,480 is to be satisfied by the issue of 4,160 shares of Fathom or cash, at the option of the company.

10. Losses carried forward for income tax purposes

The company has incurred losses to March 31, 1973 totalling \$580,000 which can be carried forward for income tax purposes to be applied against any future income of the company within the time limits prescribed by law.

11. Statutory information

In accordance with Section 122.2 of the Canada Corporations Act 1970, it is reported that during the year there were seven directors (including one former director) who received no remuneration as directors and eight officers (including one former officer) who received \$78,700 as officers. During the year three directors were also officers.

